TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 238

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

E. E. COMBS AND EDWARD EVERETT, TRUSTEES OF E. E. COMBS WELL NO. 2, EXPRESS TRUST

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR CERTIORARI FILED JULY 11, 1935

CERTIORARI GRANTED OCTOBER 14, 1935

SUPREME COURT OF THE UNITED STATES

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vs.

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Docket No. 47099

APPEARANCES:

For Petitioners,
ROBT. N. MILLER, Esq.,
M. D. WILSON, Esq.,

For Respondent,
C. H. CURL, Esq.,

DOCKET ENTRIES:

1930

Jan. 20—Petition received and filed. Taxpayer notified. (Fee paid).

Jan. 21—Copy of petition served on General Counsel.

Mar. 10—Answer filed by General Counsel.

Mar. 17—Copy of answer served on taxpayer—assigned to Circuit Calendar.

1933

July 12—Hearing set at Long Beach, Calif., week of 9/25/33.

Sept. 25—Hearing had before E. H. Va[illegible]ossan, Division 9. Submitted on merits. Stipulation of facts filed. Briefs due 10/23/33—no exchange.

Oct. 10—Transcript of hearing 9/25/33 filed.

Oct. 21—Brief filed by taxpayer.

Nov. 18—Memorandum opinion rendered—E. H. Van Fossan, Division 9. Decision will be be entered under Rule 50.

Dec. 19—Notice of settlement filed by General Counsel.

Dec. 22—Hearing set Jan. 17, 1934, under Rule 50.

1934

Jan. 1—Consent to settlement filed by taxpayer.

Jan. 12—Decision entered—Ernest H. Van Fossan, Division 9.

Apr. 6—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error field by General Counsel.

Apr. 25—Proof of service filed by General Counsel.

May 22—Agreed statement of evidence lodged.

May 22—Praecipe with proof of service thereon filed.

May 23—Agreed statement of evidence approved and ordered filed.

June 5—Order enlarging time for transmission and delivery of record to June 23, 1934, entered. [1*]

United States Board of Tax Appeals.

Docket No. 47099.

E. E. COMBS and EDWARD EVERETT, Trustees of E. E. Combs Well No. 2 Express Trust,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION.

The above-named Petitioners hereby petition for a redetermination of the deficiency set forth by the

*Page numbering appearing at the foot of page of original certified Transcript of Record.

Commissioner in his notice of deficiency, IT:AR:C-5 MN 60D, dated December 18, 1929, and as a basis of their proceeding allege as follows:

I.

The Petitioners are E. E. Combs and Edward Everett, fiduciaries, Trustees of E. E. Combs Well No. 2 Express Trust, with their residence at 1400 Pacific Avenue, Long Beach, California.

II.

The notice of deficiency, a copy of which is attached and marked Exhibit "A", was mailed to the Petitioners on December 18, 1929.

III.

The taxes in controversy are corporation income taxes as follows: [2]

1925	$2,741.95
1926	4,627.27
	$7,369.22

IV.

The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) Respondent erred in considering the trust as an association, subject to corporate income taxes.

(b) The Respondent is barred by the statute of limitations from issuing a deficiency or for assessing the proposed additional tax for the calendar year 1925.

V.

The facts upon which the Petitioner relies as the basis of this proceeding are as follows:

(a) On February 6, 1925, E. E. Combs and Edward Everett caused a trust known as E. E. Combs Well No. 2 Express Trust, to be organized, naming themselves as trustees. A copy of the Declaration of Trust is attached hereto and made a part hereof.

(b) They caused an oil lease to be transferred to themselves as trustees.

(c) Certain persons were named as beneficiaries.

(d) The Trustees had sole and exclusive power to manage the trust property.

(e) The beneficiaries had no voice or control over the affairs of the trust.

(f) There were no officers or Board of Managers. [3]

(g) The trust simply developed a single parcel of real property into oil producing property, sold it, distributed the proceeds, and terminated its existence.

(h) The trust did not engage in business.

(i) The trust was formed and operated for the sole purpose of liquidating a single parcel of real property.

(j) The trust filed a fiduciary return for the calendar year 1925, on or before March 15, 1926.

(k) The time for assessing tax against the trust expired on March 15, 1929, under the Re-

venue Act of 1926 in effect for the calendar year 1925.

(l) The Respondent did not assess the proposed additional tax or issue the deficiency letter before March 15, 1929.

(m) The Respondent is now barred from asserting a deficiency or assessing tax for 1925.

WHEREFORE, the Petitioners pray that this Board may hear the proceeding in Los Angeles, California, and determine that the trust is not taxable as an association, and that the proposed additional tax for 1925 is barred by the statute of limitations.

ROBERT N. MILLER,
922 Southern Building,
Washington, D. C.
MELVIN D. WILSON,
819 Title Insurance Bldg.,
Los Angeles, California.
GEORGE M. THOMPSON,
505 Title Insurance Bldg.
Los Angeles, California. [4]

State of California,
County of Los Angeles.—ss.

E. E. Combs and Edward Everett, being duly sworn, depose and say:

That they are the Trustees of E. E. Combs Well #2 Express Trust, the Petitioner named in the foregoing Petition; that they are authorized to

verify the Petition; that they have read the same and that the statements therein made are true.

E. E. COMBS,
EDWARD EVERETT.

Subscribed and sworn to before me this 15th day of January, 1930.

(Seal) ZELDA M. COLBY,
Notary Public in and for the County of Los Angeles, State of California. [5]

N.P. 2

EXHIBIT "A"

TREASURY DEPARTMENT
WASHINGTON

(Seal)
Office of
Commissioner of Internal Revenue

Address reply to
Commissioner of Internal Revenue Dec. 18, 1929
And refer to
E. E. Combs Well #2, Express Trust,
c/o Melvin D. Wilson,
433 South Spring Street,
Los Angeles, California.

Sirs:

In accordance with Section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the years 1925 and 1926

discloses a deficiency of $7,369.22, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

HOWEVER, IF YOU DO NOT DESIRE TO PETITION, you are requested to execute the inclosed Form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; WHEREAS IF NO AGREEMENT IS FILED, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

ROBT. H. LUCAS,
Commissioner.

By DAVID BURNET,
Deputy Commissioner.

Inclosures:
Statement
Form 866
Form 882
Form 7928-Rev. Dec. 1928. [6]

STATEMENT.

IT:AR:C-5
MN:60D

In re: E. E. Combs Well #2, Express Trust,
c/o Melvin D. Wilson,
433 South Spring Street,
Los Angeles, California.

Tax Liability

Years	Corrected Tax Liability	Tax Previously Assessed	Deficiency
1925	$2,741.95	None	$2,741.95
1926	4,627.27	None	4,627.27
Totals	$7,369.22	None	$7,369.22

Reference is made to the report of the Internal Revenue Agent in Charge, San Francisco, California, and to your protest submitted under date of December 15, 1928.

You are advised that careful consideration has been accorded your protest in connection with the agent's findings and the report on conference held May 1, 1929, in the office of the Agent in Charge.

Your contention that the taxpayer is not taxable as an association is denied, since an examination of the trust indenture and the method of doing business indicates that the organization is an association as defined by Article 1504 of Regulations 69 and subject to tax as a corporation.

Your contention for the depletion allowance as shown by your books has been allowed in so far as

it does not exceed the limitations provided in Article 221 of Regulations 69.

Your contention has been allowed in determining the profit realized on the sale of the well during the year 1926 as reflected by your books.

Accordingly, the adjustments recommended by the agent have been approved by this office and the determination of your tax liability is as follows:

1925		
Net income as disclosed by books		$48,859.06
Additions:		
1. Excessive depletion:		
Amount claimed	$24,683.36	
Amount allowed	23,091.94	1,591.42
Total		$50,450.48
		[7]
Brought forward		$50,450.48
Deduction:		
2. Drilling expenses		27,358.54
Net income as adjusted		$23,091.94

Explanation of Adjustments

1. Depletion has been allowed in accordance with Article 221 of Regulations 69. Inasmuch as 27½% of the gross income exceeds 50% of the net income without the benefit of depletion the latter amount must be used as the depletion deduction.

2. This item represents intangible drilling expenses capitalized on the books which is an allow-

able deduction under Article 223 of Regulations 69, since the taxpayer has elected to expense such items.

Computation of Tax.

Net income	$23,091.94
Less:	
Exemption	2,000.00
Balance taxable at 13%	$21,091.94
Tax liability	$ 2,741.95
Previously assessed	None
Deficiency	$ 2,741.95

1926

Net income disclosed by books	$34,276.09

The net income as disclosed by books in the above amount has been approved by this office.

Computation of Tax

Net income	$34,276.09
Less:	
Exemption	None
Balance taxable at 13½%	$34,276.09

[8]

Tax liability	$4,627.27
Previously assessed	None
Deficiency	$4,627.27

A consent which will expire December 31, 1929 except as extended by the provisions of Section

277(b) of the Revenue Act of 1926 is on file for the year 1925.

Due to the fact that the statute of limitations will presently bar any assessment of additional tax against you for the year 1925 the Bureau will be unable to afford you an opportunity under the provisions of Treasury Decision 3867, to discuss your case before mailing formal notice of the determination as provided by Section 274(a) of the Revenue Act of 1926. It is, therefore, necessary at this time, in order to protect the interests of the Government, to issue this formal notice of deficiency. [9]

EXHIBIT "B"
MEMORANDUM OF FORMATION OF EXPRESS TRUST

DATED: February 6, 1925.

PURPOSE OF TRUST:

To finance and drill a well for production and sale of oil and other hydro-carbon substances under Oil and Gas Lease, dated July 24, 1924, recorded in Book 3443, page 170, Official Records, Los Angeles County, California, on Lot One (1) Block Eighteen (18), Athens, per map recorded in Book 8, page 146 of Maps, in said County.

IDENTIFICATIONS:

Hub Oil Company, a California corporation, as Assignor;

E. E. COMBS and EDWARD EVERETT (unless named individually) as TRUSTEES; and

ALL PERSONS who may own or acquire portions of the whole beneficial interest hereunder as BENEFICIARIES.

TERMS:

ASSIGNOR has assigned to Trustees all rights of Lessee under said lease, subject to a reservation in Assignor of .065 per cent of all oil, gas and other hydro-carbon substances which may be produced and saved under said lease, and to a reservation in favor of one Henry D. Smithson of a royalty interest in said lease equal to two one-hundredths (2/100) of the interest thereunder originally held by the Assignor.

ASSIGNOR will supply to Trustee, and at site, as and when required by them, adequate for purpose for use hereunder, and build and connect complete derrick for heavy rotary drilling to depth of 5000 feet, steam engines, boilers, control head, gas trap, and tanks. The Trustees shall pay the fair market value thereof to the Assignor out of the first proceeds accruing to the Trust from the sale of the products of such well, chargeable, pro rata, against all beneficial royalty interests hereunder, notwithstanding anything hereinafter said. Title to same shall vest in Trustees upon delivery, provided, however, that in the event of an abandonment or suspension of active drilling operations for a period of sixty (60) days the Hub Oil Company shall be ipso facto revested with title to said property and leasehold rights and may take possession of the same, free and clear from any and all claims or rights arising hereunder. [10]

SHERIDAN BAILES, an oil well driller, of Long Beach, California, has entered into an agreement in writing with E. E. Combs and Edward Everett to furnish, at the site, as and when needed for immediate and continuous drilling operations and for placing well on production, heavy rotary drilling outfit, adequate for drilling to depth of 5000 feet, and all necessary drill pipe and drilling material, and to superintend all drilling and production operations to the time when the well shall be *an* commercial production, in consideration of the covenants heretofore made to him of an interest in the royalties accruing from the operation of said well, equal to twelve per cent (12%) of the whole thereof, and under which agreement the trust estate is to pay all proper labor claims incurred in the drilling and production operations and is to also pay for all drilling and production materials which are not to be supplied by the said Hub Oil Company and the said Sheridan Bailes.

BENEFICIARIES: Each will forthwith deposit with Bank of Italy, (Trust Department), Long Beach Branch, the sum set opposite his name upon his execution hereof, to the credit of the Trustees, for use by them for the payment of labor and material claims and expenses of the trust.

TRUSTEES: (a) Will hold all property and property rights, the legal title to which may vest in them hereunder, IN TRUST, pursuant hereto; (b) Shall use all monies which may be so deposited by Beneficiaries to pay for labor, casing and

other materials incident to drilling and productions operations;

(c) Shall have and exercise all of the rights and powers of the Lessee under said Lease, except as herein provided;

(d) Shall manage and protect the trust property, pay trust debts, sell and contract for the sale of all products of the well, loan to and borrow money upon the credit of the trust at prevailing rates of interest for trust purposes; may pledge the whole beneficial interest hereunder for the repayment of the same, and may sell any unsold beneficial interests in the trust as they may deem best for trust purposes. Neither of the Trustees shall be individually liable for any act which may be done or left undone by him hereunder, except wilful misconduct. Trustees shall receive no compensation as such, but, after the well is on production, E. E. Combs shall act as Production Manager at a monthly salary of $250.00; and [11]

(e) It is specifically understood and agreed that, from time to time and pursuant to a permit or permits which may be issued by the Commissioner of Corporations, the beneficial interests of E. E. Combs, as hereinafter set forth, shall be first sold by the Trustees upon such terms and conditions as the said Commissioner may permit or direct, for the purpose of raising funds to pay any and all labor and material claims arising out of drilling operations and bringing one well on commercial production not otherwise provided for from funds

so to be deposited by the beneficiaries, and that no portion of any royalties accruing to the beneficiaries hereunder shall be used for the payment of any such labor and material claims until the said beneficial interests of E. E. Combs shall be so exhausted, but the production interests of the said E. E. Combs when so sold shall share equally in all benefits of the trust with the Beneficiaries.

All proceeds of sale of well products shall be paid direct to the Bank of Italy (Long Beach Branch) or to such other bank as the Trustees, or the survivor of them, may designate, to be distributed pursuant to the terms hereof, provided, however, that such bank shall pay all claims for labor and material incident to the operation and maintenance of the said well after the same shall be on production, which shall be certified to be correct by either of the Trustees.

BENEFICIAL INTERESTS:

The whole beneficial interest of this trust represents .71333 per cent of the gross production of the well, subject to the terms hereof. Beneficiaries shall be grouped and shall be paid their respective pro rata shares of production after a pro rata deduction for the payment of lawful trust obligations, as follows:

(a) Twenty-five per cent (25%) of gross production of the well, less pro rata deductions as herein provided for, to the Beneficiaries who may deposit monies as aforesaid for trust purposes, pro rata, proportional to their respective contributions;

(b) .44333 per cent of gross production, less like deduction and subject to all of the terms, to E. E. Combs; and,

(c) .02 per cent of gross production, less like deduction, to Edward Everett. [12]

In the event of resignation, permanent absence from Los Angeles County or refusal to act of any one of the Trustees, the remaining Trustee shall be vested with all of the rights, powers and titles of the Trustees and shall continue the operations of the trust as though he had been named in the first instance as the sole Trustee.

ISSUANCE OF BENEFICIAL CERTIFICATES:

Trustees shall forthwith apply to the Commissioner of Corporations for a permit to issue and sell Beneficial Interests hereunder. No such certificates shall be issued except pursuant to the terms of any such permit. Such certificates shall be in a form to be approved by the said Commissioner and may be impounded in Escrow until a well producing oil in commercial quantities shall be brought in on said land.

IN WITNESS WHEREOF, the parties hereto have affixed their hands and seals, the day and year above mentioned.

HUB OIL COMPANY,
(By) Geo. E. Black,
President.
(By) F. G. Delaney,
Secretary.
E. E. COMBS
EDWARD EVERETT
Trustees.

BENEFICIARIES.

Name.	Address.	Amount.	Per cent of Production.
George E. Kerrigan	211 So. Cal. Ave.	$1000	1%
T. H. Emerson	Hotel Virginia (Coronada, Calif.)	$1000	1%
A. H. Waddington	(1162 Orange Ave.)	$4000	4%
Joseph H. Bowen	624 West Ocean LB	$2000	2%
E. R. Harvey	1124 Cedar LB	$5000	5%
Fred G. Gamble	3915 Dalton LA	$2000	2%
Ferol Morgan	1208 E. 2nd St. LB	$2000	2%
F. W. Hicks	4049 Locust LB	$1000	1%
Chas. L. Jackson	4815 Vista Ave.	$1000	1%
R. G. Merrill	4820 Colorado	$1000	1%
Mrs. L. E. Burson	1835 Gardena	$3000	3%
Howard H. Lipsey	208 Pine St, LB	$1000	1%
W. D. Brown	2226 Elm	$1000	1%

[13]

State of California,
County of Los Angeles—ss.

On this 6th day of February, 1925, before me P. A. Yard, a Notary Public in and for said County, personally appeared E. E. Combs and Edward Everett, known to me to be the persons whose names are subscribed to the foregoing instrument as Trustees, and acknowledged to me that they executed the same.

WITNESS my hand and official seal.

(Signed) P. A. YARD
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: United States Board of Tax Appeals. Filed Jan. 20, 1930. [14]

[Title of Court and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits the allegations contained in paragraph III of the petition.

IV. Denies the allegations of error as set forth in paragraph IV of the petition, sub-paragraphs (a) and (b).

V. Admits that the petitioner was organized under a declaration of trust dated February 6, 1925, that the petitioner acquired, developed and disposed of certain oil producing properties, but denies all other allegations of fact contained in sub-paragraphs (a), (b), (c), (d), (e), (f), (g), (h), and (i) of said paragraph V of the petition. [15]

(j). Admits that the petitioner by one of the Trustees thereof executed a return for the calendar year 1925 on fiduciary return Form No. 1041 and caused the same to be filed in the office of the Collector for the 6th District of California on March 15, 1926.

(k). Denies the allegations of sub-paragraph (k) of paragraph V of the petition and alleges that prior to the expiration of three years after the filing of said return on, to-wit, January 4, 1929, both the petitioner and the Commissioner of Internal Revenue duly consented in writing to the assessment of the amount of any income taxes due under any return made by or on behalf of the petitioner for the year ended December 31, 1925, at any time on or before December 31, 1929, except that if a notice of a deficiency in tax should be sent to the petitioner by registered mail on or before said date then the time for making any assessment as aforesaid should be extended beyond the said date by the number of days during which the Commissioner is prohibited from making an assessment and for sixty days thereafter; that the deficiency letter from which the appeal herein was taken was duly mailed to the petitioner prior to December 31, 1929, to-wit, on December 18, 1929, and the Commissioner therein determined that the petitioner is taxable as an association.

(l). Admits that the proposed deficiency for the year 1925 has not been assessed. [16]

(m). Denies the allegations contained in sub-paragraph (m) of paragraph V of the petition.

Denies generally and specifically each and every allegation contained in the taxpayers' petition not hereinbefore admitted, qualified or denied.

WHEREFORE, it is prayed that the taxpayer's appeal be denied.

(Signed) C. M. CHAREST
General Counsel,
Bureau of Internal Revenue.

Of Counsel:
F. R. SHEARER,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals. Filed Mar. 10, 1930. [17]

[Title of Court and Cause.]

Melvin D. Wilson, Esq., for the petitioners.
C. H. Curl, Esq., for the respondent.

MEMORANDUM OPINION.

VAN FOSSAN: The respondent determined deficiencies in income taxes for the year 1925 and 1926 in the amounts of $2,741.95 and $4,627.27, respectively. Petitioners protest that error was committed in considering it as an association taxable as a corporation rather than a trust taxable as such. This is the only question submitted for decision. The facts were all stipulated.

Under date of February 6, 1925, a trust was created "to finance and drill a well for production and sale of oil and other hydro-carbon [18] substances under oil and gas lease, dated July 24, 1924, renewed etc." Hub Oil Company was named as assignor and E. E. Combs and Edward Everett were

named trustees, all three parties signing the agreement. The memorandum provided that "all persons who may own or acquire portions of the whole beneficial interest hereunder" were beneficiaries.

The memorandum recites that the assignor had assigned to the trustees all rights of lessee under the lease subject to reservation to assignor of 6.5 per cent of all oil, gas and other hydro-carbons produced and subject to a reserved royalty of 2 per cent in another party.

The assignor agreed to supply the trustees certain equipment, one Sheridan Bailes had agreed in writing to furnish drilling equipment, other materials and superintend the operation of drilling the well in consideration of 12 per cent of the production, the trust to pay all labor claims and materials not otherwise provided for.

The "whole beneficial interest" in the trust was .71333 per cent of gross production. This interest was to be owned (a) 25 per cent, less deductions provided for, to beneficiaries who provide money for trust purposes, (b) .44333 per cent to E. E. Combs, (c) 2 per cent to Edward Everett.

The memorandum provided for the issuance of certificates of beneficial interest in approved legal form, such certificates to be held in escrow until a producing well is brought in. Thirteen persons were named as beneficiaries with the amount contributed and percentage owned by each, the amounts aggregating $25,000 and the percentage of ownership amounting to 25 per cent. [19]

The "Certificate of Beneficial Interest" recited that the party named was the holder of a beneficial interest under the trust agreement in the amount of a certain per cent of net production, and the same was transferable only upon the books of the trustees upon endorsement and surrender of the certificate.

The memorandum specified the duties and powers of the trustees as follows:

> (a) Will hold all property and property rights, the legal title to which may vest in them hereunder, IN TRUST, pursuant hereto;
>
> (b) Shall use all monies which may be so deposited by Beneficiaries to pay for labor, casing and other materials incident to drilling and productions operations;
>
> (c) Shall have and exercise all of the rights and powers of the Lessee under said Lease, except as herein provided;
>
> (d) Shall manage and protect the trust property, pay trust debts, sell and contract for the sale of all products of the well, loan to and borrow money upon the credit of the trust at prevailing rates of interest for trust purposes; may pledge the whole beneficial interest hereunder for the repayment of the same, and may sell any unsold beneficial interests in the trust as they may deem best for trust purposes. Neither of the Trustees shall be individually liable for any act which may be done or left undone by him hereunder, except wilful miscon-

duct. Trustees shall receive no compensation as such, but after the well is on production, E. E. Combs shall act as Production Manager at a monthly salary of $250.00, and

(e) It is specifically understood and agreed that, from time to time and pursuant to a permit or permits which may be issued by the Commissioner of Corporations, the beneficial interests of E. E. Combs, as hereinafter set forth, shall be first sold by the Trustees upon such terms and conditions as the said Commissioner may permit or direct, for the purpose of raising funds to pay any and all labor and material claims [20] arising out of drilling operations and bringing one well on commercial production not otherwise provided for from funds so to be deposited by the beneficiaries, and that no portion of any royalties accruing to the beneficiaries hereunder shall be used for the payment of any such labor and material claims until the said beneficial interests of E. E. Combs shall be so exhausted, but the production interests of the said E. E. Combs when so sold shall share equally in all benefits of the trust with the Beneficiaries.

All proceeds of sale of well products shall be paid direct to the Bank of Italy (Long Beach Branch) or to such other bank as the Trustees, or the survivor of them, may designate, to be distributed pursuant to the terms hereof, provided, however, that such bank shall pay all

claims for labor and material incident to the operation and maintenance of the said well after the same shall be on production, which shall be certified to be correct by either of the Trustees.

The provisions of the Declaration of Trust were carried out: The Hub Oil Company assigned the oil lease, mentioned in the Declaration of Trust, to the Trustees, and furnished the equipment specified in said Declaration of Trust, and received $15,000 therefor out of the proceeds from the sale of oil; Sheridan Bailes furnished the equipment and materials and services specified in the Declaration f Trust, and received 12 per cent of the gross production; Thirteen (13) persons contributed $25,000 to the Trustees in consideration of the issuance to them of 25 per cent of the net production of the well; E. E. Combs sold 9¼ per cent of the net production of the well, theretofore assigned to him, for $9,250, all of which he expended for drilling costs. He transferred 4.69 per cent of the net production to drillers and to an agent as a commission for obtaining the said lease.

A well was drilled in 1925 and produced oil throughout the remainder of 1925 and for a portion of the year 1926. In 1926, the Trustees sold [21] the lease. The trustees, in 1925 and 1926, currently distributed to the beneficiaries entitled thereto, the net proceeds from the sale of oil and from the sale of the lease. After the sale of the lease, in 1926, and the distribution of the moneys, the trust was terminated.

The beneficiaries never held a meeting. The trust had no office or place of business, no seal, no by-laws, and no official name. The trustees acquired only the one lease. They did not borrow any money or engage in any other business.

The respondent relies solely on Durfee Mineral Company, 7 B. T. A. 231. On examination, we find few points in common between the cases. In the Durfee case the creating instrument constantly refers to the organization as an "association" or "a joint stock association." The trustees were authorized to fill vacancies, select and appoint officers, conduct the business of the association, draw up and approve by-laws and amend such by-laws and the declaration of trust. "Voting privileges in the management of the business affairs of the Company" were delegated to the shareholders in the declaration of trust. Meetings of the shareholders were held. The company had a complex form of organization. The agreement provided for carrying on a general oil, gas and mineral production and marketing business in addition to selling or leasing land.

The present case presents a very different picture. There was but one, and that a very limited, enterprise authorized. The beneficiaries had no power or control. In none of the essential elements did the [22] petitioner resemble a corporation either in form or operation. The facts are comparable to those in Myers, Long & Co., 14 B. T. A. 460, where we ruled the petitioner not an association. This case has been cited with approval in many later decisions. See also Extension Oil Co., 16 B. T. A. 1028, affd. 47

Fed (2d) 65; Royal Syndicate, 20 B. T. A. 255; Ray Oil Co., 28 B. T. A. 1204.

Decision will be entered under Rule 50.

[Endorsed]: Entered Nov. 18, 1933. [23]

United States Board of Tax Appeals

Docket No. 47099

E. E. COMBS and EDWARD EVERETT, Trustees of E. E. COMBS WELL #2 EXPRESS TRUST,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION.

Pursuant to the memorandum opinion of the Board entered November 18, 1933, the respondent herein on December 19, 1933, filed a notice of settlement and proposed computation, and the petitioner on January 1, 1934, having filed an acquiescence in the computation as made by the respondent, now therefore, it is

ORDERED AND DECIDED that there are no deficiencies in income tax for the years 1925 and 1926.

Enter:

[Seal] (Signed) ERNEST H. VAN FOSSAN

Member.

[Endorsed]: Entered Jan. 12, 1934. [24]

[Title of Court and Cause.]

PETITION FOR REVIEW AND ASSIGNMENTS OF ERROR.

To the Honorable Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Now comes Guy T. Helvering, Commissioner of Internal Revenue, by his attorneys Frank J. Wideman, Assistant Attorney General, Robert H. Jackson, General Counsel, Bureau of Internal Revenue, and Hugh Brewster, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I.

That this is a proceeding for review by the United States Circuit Court of Appeals for the Ninth Circuit of a decision of the United States Board of Tax Appeals entered on November 18, 1933, Docket No. 47099, redetermining no deficiencies in income taxes due from the petitioner below for the years 1925 and 1926. [25]

That your petitioner is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States, holding office by virtue of the laws of the United States. That the respondents are individuals, and the duly appointed, qualified and acting trustees of the E. E. Combs Well #2 Express Trust, whose residence and place of business is Long Beach, California.

That the respondents herein filed their fiduciary returns of income for the years involved herein with the Collector of Internal Revenue for the Sixth District of California, within the jurisdiction of this Court.

That this petition for review is filed in pursuance of the provisions of Sections 1001-1003 of the Revenue Act of 1926, for the review of the decision of the United States Board of Tax Appeals rendered January 12, 1934, in accordance with the memorandum opinion of that Board entered on November 18, 1933.

II.

The only issue involved in this proceeding is whether the respondents were an association taxable as a corporation within the meaning of the Revenue Act of 1926.

On February 26, 1925, a trust was created to finance and drill an oil well for the production and sale of oil and other hydro-carbon substances. [26]

The trust was created and operated as follows:

The Hub Oil Company assigned an oil lease to two individuals as trustees. The assignor reserved only a right of .062 per cent of the production for himself and a royalty of 2/100 of the interest under the lease, which he originally held. The assignor was to supply the trustees with a site, derrick, engines, boilers, etc. for which the trustees were to pay the assignor their fair market value out of the first proceeds accruing to the trust. Title was to vest in the trustees upon delivery provided that if drilling operations were abandoned for a period of sixty days the Hub Oil Company was to be ipso facto revested with title to the leasehold and properties. The trustees employed a well driller on a 12% royalty basis who was to furnish certain machinery and drilling

materials and to superintend the drilling and production operations.

The trustees were to hold title to all property and property rights; to use all monies paid in by holders of beneficial interests to pay for labor, etc.; to exercise all the rights and powers of the lessee under the lease; to manage the trust property, pay trust debts, sell the products, loan to and borrow money upon the credit of the trust, and sell any unsold beneficial interest as they might deem best for trust purposes. The trustees were not liable for any act of omission or commission, except wilful misconduct, and they received no compensation. After the well was put on a production basis one of the trustees was to act as production manager at a monthly salary of $250.00. The trustees had authority to sell such [27] beneficial interests as was necessary to raise funds to pay any and all labor and material claims arising out of the drilling of one well. All the proceeds of sale of products was to be deposited in a bank to be selected by the trustees. In the event of the resignation, permanent absence from Los Angeles County, or refusal to act of one of the trustees the remaining trustee was vested with all the rights, powers and titles of the trustees and was to continue the operations of the trust. The trustees were to sell beneficial interests and issue certificates therefor in accordance with authority from the Commissioner of corporations.

The whole beneficial interest in the trust was .71333 per cent of gross production. The trust in-

strument provided for the issuance of certificates of beneficial interest under a permit to be issued by the Commissioner of Corporations. It was to be provided that such certificates might be impounded in escrow until a producing well was brought in. Beneficial certificates were issued to thirteen individuals, who contributed a total of $25,000.00, and who thereby became entitled to 25% of the production.

A well was drilled in 1925 and produced oil throughout the remainder of 1925 and for a portion of the year 1926. The trustees currently distributed to the beneficiaries entitled thereto the net proceeds from the sale of oil. The lease was sold in 1926, the net proceeds of the sale were distributed and the trust terminated. [28]

Your petitioner herein held respondents to be an association taxable as a corporation within the meaning of Section 2(a)(2) of Part IV of the Revenue Act of 1926 and Article 1504 of Regulations 69. and determined deficiencies in income taxes of $2,741.95 for the year 1925 and $4,627.27 for 1926.

The Board of Tax Appeals held that the respondents were not taxable as a corporation and that there is no deficiency in taxes for either of the years 1925 and 1926.

III.

Your petitioner desires to obtain a review of the aforementioned decision of the United States Board of Tax Appeals by the United States Circuit Court of Appeals for the Ninth Circuit.

Your petitioner's assignments of error are as follows:

(1) The Board of Tax Appeals erred in holding and deciding that there is no deficiency in income taxes due from these respondents for the years 1925 and 1926.

(2) The Board erred in holding and deciding that, under the facts stipulated before the Board respondents did not resemble a corporation either in form or operation.

(3) The Board erred in holding and deciding that the associating together of the holders of the beneficial interests of the respondents herein, together with their subscription to the fund for the liquidation of the lawful obligations of the trust, and cost of labor, materials and production operations and their [29] proportionate sharing of the profits therefrom, did not constitute them an association, taxable as a corporation.

(4) The Board erred in not holding and deciding that respondents constituted an association taxable as a corporation.

WHEREFORE, the Commissioner petitions that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit, that a transcript of the record be prepared in accordance with the law and with the rules of the said Court and transmitted to the Clerk of the said Court for filing, and that appropriate action be taken to the end that the er-

rors complained of may be reviewed and corrected by said Court.

HB/mhk 4/6/34

FRANK J. WIDEMAN,
Assistant Attorney General.
(Signed) ROBERT H. JACKSON
General Counsel,
Bureau of Internal Revenue.

Of Counsel:
HUGH BREWSTER
Special Attorney,
Bureau of Internal Revenue. [30]

VERIFICATION OF PETITION FOR REVIEW.

United States of America,
District of Columbia—ss.

Hugh Brewster, being duly sworn, says that he is a Special Attorney of the Bureau of Internal Revenue, and as such is duly authorized to verify the foregoing petition for review; that he has read said petition and is familiar with the contents thereof; that said petition is true of his own knowledge except as to the matters therein alleged on information and belief, and as to those matters he believes it to be true.

(S) HUGH BREWSTER

Sworn and subscribed to before me this 6 day of ....., 1934.

HB/mhk 4/6/34

(S) GEORGE W. KREIS
Notary Public, District of Columbia.
My commission expires Nov. 16, 1937.

[Endorsed]: United States Board of Tax Appeals. Filed Apr. 5, 1934. [31]

[Title of Court and Cause.]

NOTICE OF FILING PETITION FOR REVIEW

To: Melvin D. Wilson,
c/o Miller, Chevalier, Peeler & Wilson,
819 Title Insurance Building,
Los Angeles, California.

You are hereby notified that the Commissioner of Internal Revenue did, on the 6th day of April, 1934, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 6th day of April, 1934.

(Signed) ROBERT H. JACKSON
General Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 10th day of April, 1934.

MELVIN D. WILSON
Attorney for respondents on review.

HB/mhk 3/6/34

[Endorsed]: United States Board of Tax Appeals. Filed Apr. 25, 1934. [32]

In the United States Circuit Court of Appeals
for the Ninth Circuit.

BTA No. 47099.

GUY T. HELVERING, Commissioner of
Internal Revenue,

Petitioner,

v.

E. E. COMBS and EDWARD EVERETT,
Trustees of E. E. Combs Well #2
Express Trust,

Respondent.

STATEMENT OF EVIDENCE

The following is a statement of the evidence in the above-entitled cause. This cause came on for hearing before the Honorable Ernest H. Van Fossen, Member of the United States Board of Tax Appeals, on September 25, 1933. Melvin D. Wilson, Esq., appeared for the petitioner, and E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue, appeared for the respondent. All the facts were stipulated and are as follows:

I.

Attached hereto and marked Exhibit "A" is the Memorandum of Formation of Express Trust, under which this Trust was organized, and under which it functioned throughout its existence. [33]

II.

Attached hereto and marked Exhibit "B" is copy of the form of Certificate of Beneficial Interest, issued by the Trustees.

III.

That the provisions of the Declaration of Trust were carried out; The Hub Oil Company assigned the oil lease, mentioned in the Declaration of Trust, to the Trustees, and furnished the equipment specified in said Declaration of Trust, and received $15,000 therefor out of the proceeds from the sale of oil; Sheridan Bailes furnished the equipment and materials and services specified in the Declaration of Trust, and received 12 per cent of the gross production; thirteen (13) persons contributed $25,000 to the Trustees in consideration of the issuance to them of 25 per cent of the net production of the well; E. E. Combs sold 9¼ per cent of the net production of the well, theretofore assigned to him, for $9,250, all of which he expended for drilling costs. He transferred 4.69 per cent of the net production to drillers and to an agent as a commission for obtaining the said lease.

IV.

A well was drilled in 1925 and produced oil throughout the remainder of 1925 and for a portion of the year 1926. In 1926, the Trustees sold the lease. The Trustees, in 1925 and 1926, currently distributed to the beneficiaries entitled thereto, the net proceeds from the sale of oil and from the sale of the lease. After the sale of the lease, in 1926, and the distribution of the moneys, the Trust was terminated. [34]

V.

The beneficiaries never held a meeting. The Trust had no office or place of business; no seal;

no by-laws; and no official name. The Trustees acquired only the one lease. They did not borrow any money or engage in any other business.

VI.

The statute of limitations issue is waived or conceded by the taxpayer.

EXHIBIT "A"

MEMORANDUM OF FORMATION OF EXPRESS TRUST

Dated: February 6, 1925.

PURPOSE OF TRUST:

To finance and drill a well for production and sale of oil and other hydro-carbon substances under Oil and Gas Lease, dated July 24, 1924, recorded in Book 3443, page 170, Official Records, Los Angeles County, California, on Lot One (1) Block Eighteen (18), Athens, per map recorded in Book 8, page 146 of Maps, in said County.

IDENTIFICATIONS:

Hub Oil Company, a California corporation, as Assignor:

E. E. COMBS and EDWARD EVERETT (Unless named individually) as TRUSTEES; and, [35]

ALL PERSONS who may own or acquire portions of the whole beneficial interest hereunder as BENEFICIARIES.

TERMS:

ASSIGNOR has assigned to Trustees all rights of Lessee under said lease, subject to a reservation in Assignor of .065 per cent of all oil, gas and other hydro-carbon substances which may be produced and saved under said lease, and to a reservation in favor of one Henry D. Smithson of a royalty interest in said lease equal to two one-hundredths (2/100) of the interest thereunder originally held by the Assignor.

ASSIGNOR will supply to Trustees, and at site, as and when required by them, adequate for purpose for use hereunder, and build and connect complete derrick for heavy rotary drilling to depth of 5,000 feet, stem engines, boilers, control head, gas trap, and tanks. The Trustees shall pay the fair market value thereof to the Assignor out of the first proceeds accruing to the Trust from the sale of the products of such well, chargeable, pro rata, against all beneficial royalty interests hereunder, notwithstanding anything hereinafter said. Title to same shall vest in Trustees upon delivery, provided, however, that in the event of an abandonment or suspension of active drilling operations for a period of sixty (60) days the Hub Oil Company shall be ipso facto revested with title to said property and leasehold rights [36] and may take possession of the same, free and clear from any and all claims or rights arising hereunder.

SHERIDAN BAILES, an oil well driller, of Long Beach, California, has entered into an agree-

ment in writing with E. E. Combs and Edward Everett to furnish, at the site, as and when needed for immediate and continuous drilling operations and for placing well on production, heavy rotary drilling outfit, adequate for drilling to depth of 5,000 feet, and all necessary drill pipe and drilling material, and to superintend all drilling and production operations to the time when the well shall be on commercial production, in consideration of the covenants heretofore made to him of an interest in the royalties accruing from the operation of said well, equal to (12%) twelve per cent of the whole thereof, and under which agreement the trust estate is to pay all proper labor claims incurred in the drilling and production operations and is to also pay for all drilling and productions materials which are not to be supplied by the said Hub Oil Company and the said Sheridan Bailes.

BENEFICIARIES: Each will forthwith deposit with Bank of Italy, (Trust Department), Long Beach Branch, the sum set opposite his name upon his execution hereof, to the credit of the Trustees, for use by them for the payment of labor and material claims and expenses of the trust.

TRUSTEES: (a) Will hold all property and property rights, the legal title to which may vest in them hereunder, IN TRUST, pursuant hereto; [37]

(b) Shall use all monies which may be so deposited by Beneficiaries to pay for labor, casing and other materials incident to drilling and productions operations;

(c) Shall have and exercise all of the rights and powers of the Lessee under said Lease, except as herein provided;

(d) Shall manage and protect the trust property, pay trust debts, sell and contract for the sale of all products of the well, loan to and borrow money upon the credit of the trust at prevailing rates of interest for trust purposes; may pledge the whole beneficial interest hereunder for the repayment of the same, and may sell any unsold beneficial interests in the trust as they may deem best for trust purposes. Neither of the Trustees shall be individually liable for any act which may be done or left undone by him hereunder, except wilful misconduct. Trustees shall receive no compensation as such, but, after the well is on production, E. E. Combs shall act as Production Manager at a monthly salary of $250.00; and

(e) It is specifically understood and agreed that, from time to time and pursuant to a permit or permits which may be issued by the Commissioner of Corporations, the beneficial interests of E. E. Combs, as hereinafter set forth, shall be first sold by the Trustees upon such terms and conditions as the said Commissioner may permit or direct, for the purpose of raising funds to pay any and all labor and material claims arising out of drilling operations and bringing one [38] well on commercial production not otherwise provided for from funds so to be deposited by the beneficiaries, and that no portion of any royalties accruing to the beneficiaries hereunder shall be used for the payment of any such

labor and material claims until the said beneficial interests of E. E. Combs shall be so exhausted, but the production interests of the said E. E. Combs when so sold shall share equally in all benefits of the trust with the beneficiaries.

All proceeds of sale of well products shall be paid direct to the Bank of Italy (Long Beach Branch) or to such other bank as the Trustees, or the survivor of them, may designate, to be distributed pursuant to the terms hereof, provided, however, that such bank shall pay all claims for labor and material incident to the operation and maintenance of the said well after the same shall be on production, which shall be certified to be correct by either of the Trustees.

BENEFICIAL INTERESTS:

The whole beneficial interest of this trust represents .71333 per cent of the gross production of the well, subject to the terms hereof. Beneficiaries shall be grouped and shall be paid their respective pro rata shares of production after a pro rata deduction for the payment of lawful trust obligations, as follows: [39]

(a). Twenty-five per cent (25%) of gross production of the well, less pro rata deductions as herein provided for, to the Beneficiaries who may deposit monies as aforesaid for trust purposes, pro rata, proportional to their respective contributions:

(b) .44333 per cent of gross production, less like deduction and subject to all of the terms, to E. E. Combs; and,

(c) .02 per cent of gross production, less like deduction, to Edward Everett.

In the event of resignation, permanent absence from Los Angeles County or refusal to act of any one of the Trustees, the remaining Trustee shall be vested with all of the rights, powers and titles of the Trustees and shall continue the operations of the trust as though he had been named in the first instance as the sole Trustee.

ISSUANCE OF BENEFICIAL CERTIFICATES:

Trustees shall forthwith apply to the Commissioner of Corporations for a permit to issue and sell Beneficial Interests hereunder. No such certificates shall be issued except pursuant to the terms of any such permit. Such certificates shall be in a form to be approved by the said Commissioner and may be impounded in Escrow until a well producing oil in commercial quantities shall be brought in on said land. [40]

IN WITNESS WHEREOF, the parties hereto have affixed their hands and seals, the day and year above mentioned.

HUB OIL COMPANY,
(By) Geo. E. Black,
President.
(By) F. G. Delaney,
Secretary.
E. E. COMBS
EDWARD EVERETT
Trustee.

BENEFICIARIES

Name	Address	Amount	Per cent of Production
George E. Kerrigan	211 So. Cal. Ave.	$1000	.1%
T. H. Emerson	Hotel Virginia (Coronado, Calif.	$1000	1%
A. H. Waddington	(1162 Orange Ave.)	$4000	4%
Joseph H. Bowen	624 West Ocean LB	$2000	2%
E. R. Harvey	1124 Cedar LB	$5000	5%
Fred G. Gamble	3915 Dalton LA	$2000	2%
Ferol Morgan	1208 E. 2nd St. LB	$2000	2%
F. E. Hicks	4049 Locust LB	$1000	1%
Chas. L. Jackson	4815 Vista Ave	$1000	1%
R. G. Merrill	4820 Colorado	$1000	1%
Mrs. L. E. Burson	1835 Gardena	$3000	3%
Howard H. Lipsey	208 Pine St. LB	$1000	1%
W. D. Brown	2226 Elm	$1000	1%

[41]

"EXHIBIT B".

CERTIFICATE OF BENEFICIAL INTEREST.

E. E. Combs and Edward Everett, herein designated as Trustees, hereby certify that EDWARD EVERETT is the holder of a beneficial interest under that certain agreement for the formation of an express trust, made on the 6th day of February, 1925, and relating to the financing and drilling of a well for the production of oil and other hydro carbon substances on Lot 1, Block 18, Athens, Los Angeles County, California, which beneficial interest entitles the said Edward Everett to One-half of One per cent of the net production of any well which may be drilled upon the said lot under the said trust, subject to all of the agreements and conditions thereof.

The beneficial interest evidenced hereby is transferable only upon the books of the Trustees upon endorsement and surrender of this certificate.

Dated at Long Beach, California, this 17th day of April, 1925.

(Signed) E. E. COMBS
(Signed) EDWARD EVERETT
Trustees [42]

The foregoing evidence is all of the material evidence adduced at the hearing before the Board of Tax Appeals, and the case is approved by the undersigned, Robert H. Jackson, General Counsel, Bureau of Internal Revenue, as attorney for the Commisioner of Internal Revenue.

(Signed) ROBERT H. JACKSON
General Counsel,
Bureau of Internal Revenue.

The foregoing is all of the material evidence adduced at the hearing before the Board of Tax Appeals, and the same is approved by the undersigned, as attorney for respondent on review.

MELVIN D. WILSON
Attorney for Respondent on Review. [43]

Approved and Ordered Filed, May 23, 1934.

(S) ERNEST H. VAN FOSSAN

Member,

United States Board of Tax Appeals.

[Endorsed]: United States Board of Tax Appeals. Lodged May 22, 1934.

[Endorsed]: United States Board of Tax Appeals. Filed May 23, 1934.[44]

[Title of Court and Cause.]

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Ninth Circuit, heretofore filed by the Commissioner of Internal Revenue.

1. Docket entries of the proceedings before the Board.

2. Pleadings before the Board,

   (a) Petition, including annexed copy of deficiency letter.

   (b) Answer.

3. Memorandum opinion and decision of the Board.

4. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.

5. Statement of the evidence as settled and allowed.

6. Orders enlarging time for the preparation of the evidence and for the transmission and delivery of the record not included in record.

7. This praecipe.

HB/mhk 4/28/34

(Signed) ROBERT H. JACKSON
General Counsel,
Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 14th day of May, 1934.

MELVIN D. WILSON
Attorney for Respondent.

[Endorsed]: United States Board of Tax Appeals. Filed May 22, 1934. [45]

United States Board of Tax Appeals
Washington

Docket No. 47099

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

v.

E. E. COMBS and EDWARD EVERETT,
Trustees of E. E. COMBS WELL # 2
EXPRESS TRUST,
Respondent.

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 45, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 13th day of June, 1934.

[Seal] B. D. GAMBLE
Clerk,
United States, Board of Tax Appeals.

[Endorsed]: No. 7523. United States Circuit Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. E. E. Combs and Edward Everett, Trustees of E. E. Combs Well No. 2, Express Trust, Respondents. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed June 18, 1934.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

49 In United States Circuit Court of Appeals for the Ninth Circuit

No. 7523

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

E. E. COMBS AND EDWARD EVERETT, TRUSTEES, ETC., RESPONDENT

Before WILBUR and GARRECHT, C. J. J., and CAVANAH, D. J.

Order of submission

January 24, 1935

Ordered petition to review in above cause argued by Mr. Lucius A. Buck, Special Assistant to the Attorney General, counsel for petitioner, and by Mr. Dana Latham, counsel for respondent, and submitted to the court for consideration and decision.

50 In United States Circuit Court of Appeals

[Title omitted.]

Order directing filing of opinion and filing and recording of judgment

By direction of the court, ordered that the typewritten opinion this day rendered by this court in above cause be forthwith filed by the clerk and that a judgment be filed and recorded in the minutes of this court in accordance with the opinion rendered.

51 In United States Circuit Court of Appeals for the Ninth Circuit

No. 7523

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

E. E. COMBS AND EDWARD EVERETT, TRUSTEES OF E. E. COMBS WELL NO. 2, EXPRESS TRUST, RESPONDENTS

Upon Petition to Review an Order of the United States Board of Tax Appeals

Before WILBUR and GARRECHT, Circuit Judges, and CAVANAH, District Judge

Opinion

WILBUR, *Circuit Judge:*

April 11, 1935

The Commissioner of Internal Revenue determined a deficiency in the tax of the respondents for the years 1925 and 1926 amounting to $7,369.22. This deficiency it appears was assessed upon the theory

that the respondents were acting as an association and therefore taxable under the Revenue Act of 1926, §2 (a), 44 Stat. 9, as interpreted by Treasury Regulations 69, promulgated under that act, arts, 1502, 1504. The Board of Tax Appeals reversed the decision of the Commissioner upon the ground that the respondents were not an association and the Commissioner brings this petition to review the act of the Board of Tax Appeals. The question as to whether or not organizations are taxable associations under the revenue act is one that has been frequently before the courts and is not free from difficulty. The various decisions have been collected and discussed in a number of recent cases, Reinecke v. Kaempfer, 72 F. (2d) 469; Twin Bell Oil Syndicate v. Helvering, 70 F. (2d) 402; Hecht v. Malley, 265 U. S. 144; Commissioner v. Brouillard, 70 F. (2d) 154; Burk-waggoner Oil Ass'n v. Hopkins, 269 U. S. 110. We think it
52 unnecessary to enter into an extended discussion of the various decisions of the courts of appeals dealing with the question, or to attempt to establish the proper rule for determining the question of tax liability. The tendency of the recent cases is to deal with the facts of the particular case rather than to attempt to define the term "Association" more precisely than is done by the regulations of the Treasury Department. So stated Judge Sparks, speaking for the Circuit Court of Appeals in the Seventh Circuit in Tyson v. Com'r., 68 F. (2d) 584 (in February 1934), as follows:

"The trend of these decisions seems to be to look to the actual activities of the entity first, rather than to its form or possible powers."

So also is the statement of Judge Alschuler, speaking for the same court in Reinecke v. Kaempfer, supra (in June 1934), where he said:

"We are satisfied that the similitude referred to is not in those essentials which distinctly stamp the entity as a corporation, but rather in the business carried on and the manner of its transaction."

Judge Wilson, speaking for the Circuit Court of Appeals for the First Circuit, dealt with this matter in a recent opinion (Commissioner v. Kelly, 74 F. (2d) 71) saying,

"The courts have also said that in determining whether a trust is taxable as a corporation, substance rather than form is to be regarded; but each case must be determined on its own facts."

In the latter case (Commissioner v. Kelly, supra) Judge Wilson reviewed the decisions on this subject and deduced the conclusion that,

"To constitute a trust an association, and taxable as a corporation, there must be a body of persons associated together who are (1) actually carrying on business for profit, and (2) under the usual forms and procedure of corporations. Both conditions must be present."

53 In Twin Bell Oil Syndicate v. Helvering, 70 F. (2d) 402, we considered the proper interpretation of the statute and rules of the Treasury Department concerning the taxability of as-

sociations there involved and held that the Twin Bell Oil Syndicate was such an association. Judge Sawtelle, speaking for the court said,

"• • • we are impelled to the conclusion that the taxpayer was engaged in business; that its organization was of a quasi corporate character, and that as a consequence, it was an 'association' and should be taxed as a corporation under the provisions of the Revenue Act of 1926 and the Treasury Regulations promulgated thereunder."

This case was reversed by the Supreme Court on other grounds (December 3, 1934), 55 Sup. Ct. 174, 75 L. Ed. 183.

It is agreed that one of the tests for determining whether or not a trust is so organized as to constitute an association within the meaning of the taxing laws is whether or not the trustees are authorized to conduct business and do so. Inasmuch as the purpose of the act is to treat associations, corporations, joint-stock companies and insurance companies on a basis distinct and separate from that applicable to trusts or copartnerships, it is clear that while a trust may be organized so that the trustees can do business, their powers, duties, obligations and methods of doing business and the relationship of the trustees to the beneficiaries, must in some degree correspond to the similar duties and obligations of directors and stockholders of a corporation in order to make the trust taxable as an association. The first test as to whether or not the trust is one to do business as distinguished from one for merely holding investments for the beneficiaries and for the transaction only of the incidental business essential to holding and maintaining the trust property so as to realize an income therefrom is a relatively simple one, while the second test as to whether or not the trust is so organized as to constitute it a quasi corporation or association because of its methods of doing business and its organization therefor, is a more difficult one involving more detailed consideration of the plan of operation. As we understand the respondents, they do not question that the trust therein was doing business, but they contend that they do not meet the second test. They claim that they "were neither organized nor did they operate in any sense of the word along
54 the modes, methods, and manners ordinarily employed by corporations." With these contentions in mind, we will state more in detail the facts concerning the trust and the business conducted thereunder by the respondents.

The Hub Oil Company was the owner of a certain oil lease on a town lot of Athens, California, which lease was subject to a royalty reserved to the lessor. E. E. Combs and Edward Everett were desirous of developing the property in conjunction with the Hub Oil Company and Sheridan Bailes, an oil-well driller. Under date of February 6, 1925, a "Memorandum of Formation of Express Trust" was drawn up and signed by the parties, which had for its purpose "to finance and drill a well for production and sale of oil and other hydrocarbon substances" under the oil lease owned

by the Hub Oil Company. The trust agreement recited that the Hub Oil Company, as assigner, had transferred to E. E. Combs and Edward Everett, as trustees, all its right as lessee under the lease, subject to a reservation of a percentage of the oil, gas, and other hydrocarbon substances which may be produced and saved under said lease. The assignor also agreed to furnish a derrick for drilling an oil well, which was to be paid for out of production. The trust agreement also recited that a contract had been entered into by Combs and Everett with Bailes for sinking a well. By the terms of the contract Bailes was to furnish the necessary tools for drilling the well and to superintend all drilling and production operations for a percentage of the oil produced. Combs and Everett as trustees, were to pay for the cost of the labor, for the oil-well casing and for the incidental supplies needed in sinking the well. To proceed with the development of the property it was only necessary to secure the money to pay for the labor costs, the oil-well casing and incidental supplies. In order to secure this money the beneficial interest in the trust was divided into shares and twenty-five shares, each representing one percent of the production less deduction for expenses, were sold for $1,000 each. The trust memorandum stated that the "whole beneficial interest of this trust represents .71333 percent of the gross production of the well, subject to the terms hereof." This interest was to be owned as follows: (1) 25% by beneficiaries providing money for trust purposes; (2) .44333 percent by E. E. Combs; and (3) .02 percent by Edward Everett. By
55 the terms of the trust agreement E. E. Combs was required to sell such portion of his beneficial interest as was needed, over and above the amounts received from the twenty-five shares, for the completion of the well. Upon the completion of the well it was provided that the moneys derived from the sale of oil produced therefrom were to be paid into a bank named in the trust agreement which was to disburse the moneys in payment of the operating expenses and distribute the balance to the beneficiaries in proportion to their beneficial interest. The trust was terminated after the well had been producing for two years by the sale of the interest of the trustees and the distribution of the proceeds to the beneficiaries in accordance with their several interests.

The trust agreement gave the two trustees large powers over the property of the trust similar to those of a board of directors of a corporation, but they had no seal, no principal place of business. There was no provision in the trust agreement for meetings of the trustees or the beneficiaries. The latter had no control over the trustees and no participation in the selection of the trustees or their successors. As above stated, the business necessary to develop the lot for oil production had been largely completed by Combs and Everett before the trust was formed. The sale of the twenty-five shares (25% of the beneficial interest) was required to secure the needed capital for drilling the well. Thereafter the trustees had little to do except to arrange for the care of the well and the marketing of the

oil. There was no authority in the trust agreement for conducting a general oil development or oil-producing business or to drill more than one well under the lease held by the trustees.

The respondents point out that the trust agreement made no provision for the election of trustees annually or otherwise. Upon the death, resignation, or refusal of one to act, the other was authorized to act alone. There were no corporate officers, no bylaws, no corporate or association name. While the question involved is a close one not free from difficulty we conclude that the Board of Tax Appeals was right in holding that the organization was not an association within the meaning of the Revenue Act but rather that it was a trust, taxable as such. Coleman-Gilbert Associates v. Commissioner, decided Feb. 27, 1935, C. C. A. 1, Prentice-Hall Federal Tax Service, 1935, p. 889.

Order affirmed.

(Endorsed:) Opinion. Filed April 11, 1935. Paul P. O'Brien, Clerk.

56 In United States Circuit Court of Appeals for the Ninth Circuit

No. 7523

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

E. E. COMBS AND EDWARD EVERETT, TRUSTEES, RESPONDENTS

Judgment

Filed April 11, 1935

Upon petition to review an Order of the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was duly submitted:

On Consideration Whereof, It is now here ordered and adjudged by this court that the Order of the said Board of Tax Appeals in this cause be, and hereby is, affirmed.

[File endorsement omitted.]

57 [Clerk's Certificate to foregoing transcript omitted in printing.]

58 Supreme Court of the United States

Order allowing certiorari

Filed October 14, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Ninth Circuit is granted, and the case is assigned for argument immediately following No. 108.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(Endorsement on cover:) File No. 39792. U. S. Circuit Court of Appeals, Ninth Circuit. Term No. 238. Guy T. Helvering, Commissioner of Internal Revenue, petitioner, vs. E. E. Combs and Edward Everett, Trustees of E. E. Combs Well No. 2, Express Trust. Petition for a writ of certiorari and exhibit thereto. Filed July 11, 1935. Term No. 238 O. T. 1935.

U. S. GOVERNMENT PRINTING OFFICE: 1935